

NCUA LETTER TO CREDIT UNIONS

**NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22314**

DATE: May 2004 **LETTER NO.: 04-CU-08**
TO: Federally Insured Credit Unions
SUBJ: Credit Union Financial Trends for the First Quarter of 2004
**ENCL: Financial Trends in Federally Insured Credit Unions
January 1 – March 31, 2004**

DEAR BOARD OF DIRECTORS:

Enclosed is a report highlighting credit union financial trends for the first quarter of 2004. We based our analysis on data compiled from the first quarter 2004 call reports submitted by all federally insured credit unions. We are providing this information to keep you informed of current conditions and trends in the credit union industry.

Thank you for your cooperation in providing this data.

Sincerely,

/S/

JoAnn Johnson
Chairman

Enclosure

FINANCIAL TRENDS IN FEDERALLY INSURED CREDIT UNIONS

January 1 – March 31, 2004

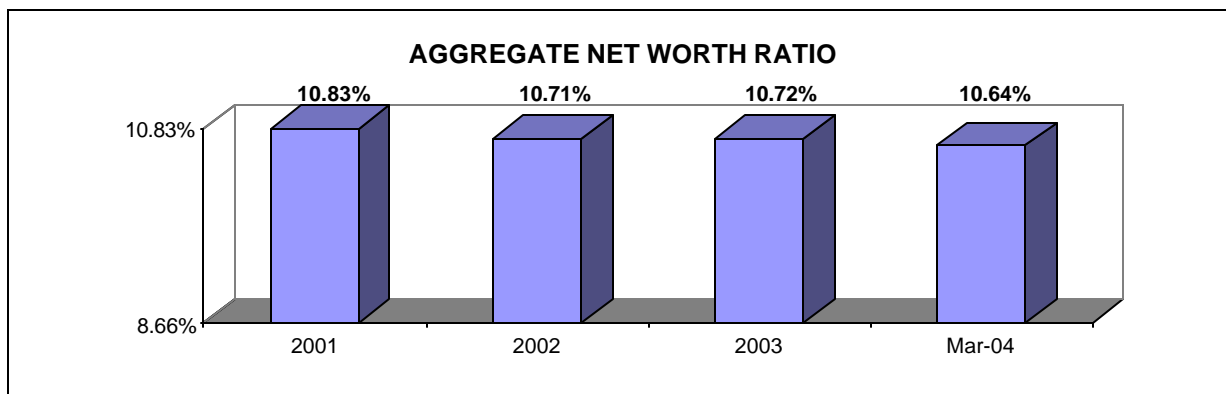
HIGHLIGHTS

This report summarizes the trends of all federally insured credit unions that reported as of March 31, 2004.

- ◆ **Assets** increased \$17.1 billion, or 2.80%. This equates to an annualized asset growth rate of 11.20%.
- ◆ **Net Worth** increased \$1.4 billion or 2.09%. The Net Worth to assets ratio decreased from 10.71% to 10.64%.
- ◆ **Loans** increased \$4.0 billion, or 1.07%. The loan to share ratio decreased from 71.19% to 69.97%.
- ◆ **Shares** increased \$14.9 billion, or 2.83%.
- ◆ **Cash on hand, cash on deposit, cash equivalents, plus short-term investments (less than 1 year)** increased \$23.1 billion, or 15.51%.
- ◆ **Long-term investments (over 1 year)** decreased \$840.4 million, or 0.78%.
- ◆ **Profitability**, as measured by return on average assets, decreased from 0.99% to 0.90%, but remains strong.
- ◆ **Delinquent** loans as a percentage of total loans decreased from 0.77% to 0.68%.

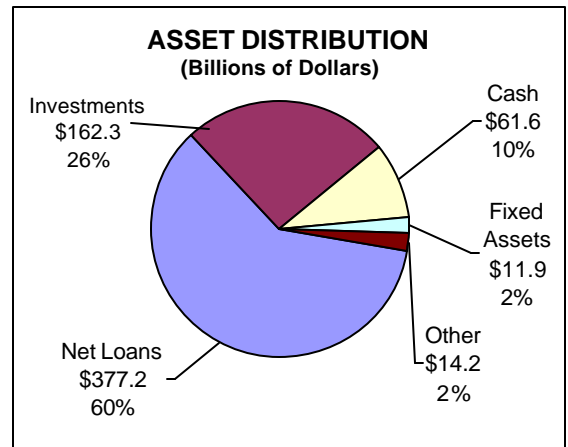
CAPITAL

Total Net Worth increased \$1.4 billion (2.09%) during the first quarter of 2004. The aggregate net worth to total assets ratio decreased from 10.71% at the end of 2003 to 10.64% as of March 31, 2004, as annualized asset growth of 11.20% outpaced annualized net worth growth of 8.35%. The average net worth ratio among individual credit unions decreased from 13.32% at the end of 2003 to 13.20% as of March 31, 2004.



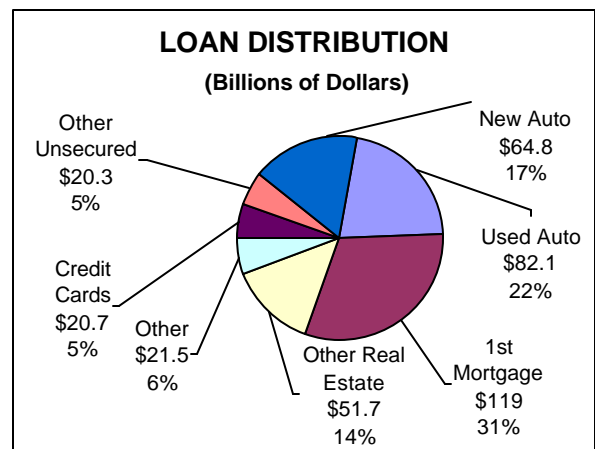
ASSET QUALITY

LOAN TRENDS: All loan categories experienced growth except for Unsecured Credit Card Loans and All Other Unsecured Loans. Loan growth of 4.28% (annualized) resulted in an increase in total loans of \$4.0 billion. Share growth was higher than loan growth, causing the loan to share ratio to decrease slightly from 71.19% in 2003 to 69.97% in the first quarter of 2004. Growth in the various loan categories is as follows:

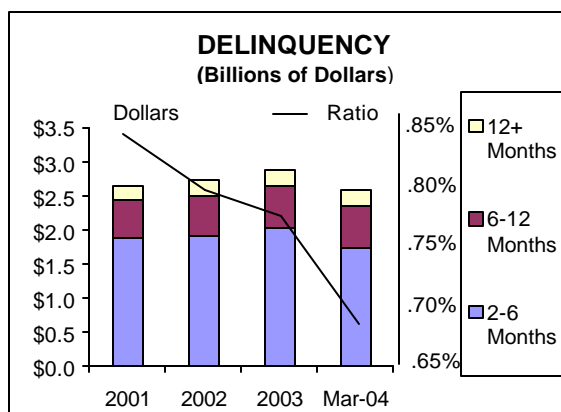


Loan Category	2003 Balance In Billions	March 2004 Balance In Billions	Growth In Billions	Growth Rate
Unsecured Credit Card	\$21.7	\$20.7	-\$1.0	-4.64%
All Other Unsecured	\$20.8	\$20.3	-\$0.5	-2.60%
New Vehicle	\$63.8	\$64.8	\$1.1	1.68%
Used Vehicle	\$81.2	\$82.1	\$0.9	1.15%
First Mortgage Real Estate	\$117.5	\$119	\$1.5	1.23%
Other Real Estate	\$50.1	\$51.7	\$1.7	3.34%
Leases Receivable	\$1.5	\$1.5	\$0.0	2.75%
All Other	\$19.5	\$19.9	\$0.4	2.09%

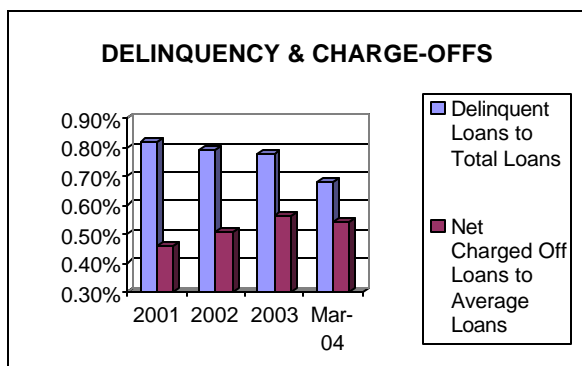
First mortgage real estate loans account for 31.30% (\$119 billion) of all loans. Loans held for sale increased 41.65%, from \$414 million to \$1.4 billion.



DELINQUENCY TRENDS: Delinquent loans decreased 9.59% (\$275.4 million). The delinquent loans to total loans ratio also declined from 0.77% at the end of 2003 to 0.68% at the end of the first quarter 2004. The decline in delinquency exceeded the increase in loans charged off in the first quarter.



On an annualized basis, loan dollars charged off increased 3.94% (\$92.3 million), whereas recoveries on charged off loans increased 16.96% (\$54.6 million). This resulted in net charged off loans decreasing by 4.86% (\$237.7 million). The net charged off to average loan ratio declined from 0.56% to 0.54% in the first quarter of 2004.



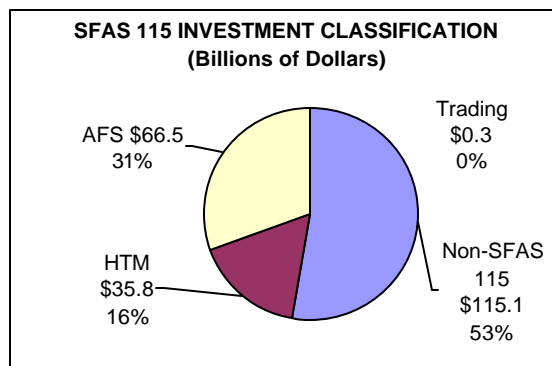
INVESTMENT TRENDS: Cash on hand, cash on deposit, and cash equivalents increased 19.73% (\$10.1 billion). These combined categories, along with investments with maturities of less than one year, increased 15.51% (\$23.1 billion).

Investments with maturities greater than a year decreased 0.78% (\$840.4 million).

Non-SFAS 115 investments (including cash on deposit and cash equivalents) increased 11.51% (\$11.9 billion) to \$115.1 billion.

Held-to-maturity investments decreased 2.05% (\$751 million). *Available-for-sale* investments increased 1.44% (\$946 million). Trading securities increased 6.72% (\$17.5 million).

At the end of the first quarter of 2004, SFAS 115 investments made up 47% of the investment portfolio. Non-SFAS 115 investments, cash on deposit, and cash equivalents accounted for 53% of the portfolio.



The following table compares the changes in the maturity structure of the investment portfolio over the past year:

Investment Maturity or Repricing Interval	% of Total Investments 2003	% of Total Investments March 2004
Less than 1 year	47.43%	50.65%
1 to 3 years	34.15%	31.83%
3 to 10 years	16.91%	16.25%
Greater than 10 yrs	1.51%	1.27%

EARNINGS

Sustained asset growth and low market interest rates continue to impact income. Total net income decreased 3.36% (\$193.6 million). The return on average assets decreased from 0.99% at the end of 2003 to 0.90%. The net interest margin declined to 3.33%. Operating expenses to average assets declined by four basis points to 3.19%. The Provision for Loan Loss Expense and non-operating income levels remained stable.

Ratio (% Ave. Assets)	As of 2003	As of March 2004	Effect on ROA
Net Interest Margin	3.41%	3.33%	- 8bp
+ Fee & Other Inc.	1.12%	1.04%	- 8bp
- Operating Expenses	3.23%	3.19%	+ 4bp
- PLL	0.35%	0.33%	+ 2bp
+ Non-Opr. Income	0.04%	0.04%	+ 0bp
= ROA	0.99%	0.90%	- 9bp

ASSET/LIABILITY MANAGEMENT

SHARE TRENDS: Total shares increased 2.83% (\$14.9 billion) in the first quarter, compared to 9.11% in 2003.

OVERALL LIQUIDITY TRENDS: In the first quarter of 2004, credit unions had approximately 18.57% of total assets in cash and short-term investments, compared to 17.07% at the end of 2003. Net long-term assets (defined as assets with maturities or repricing intervals greater than 3 years - 5 years for real estate loans), equaled 25.03% of total assets at the end of the first quarter, compared to 25.33% at the end of 2003.

INTEREST RATE RISK: Interest rates have been at historically low levels for enough time to cause credit union assets to reprice downward and result in near record low net interest margins. If interest rates rise, credit unions holding significant portions of longer term, fixed-rate assets could see even lower net interest margins, squeezed earnings, and reduced net worth.

CONCLUSION: Financial performance of the industry remains strong despite the challenges presented by the low interest rate environment. Credit unions need to remain vigilant in monitoring the impact of changing interest rates and make any needed adjustments to maintain an acceptable level of risk.